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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

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August 9, 2001

EX PARTE

Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

EX PARTE OR LATE FILED

CC: Docket Nos. 96-45; 98-171; 90-571; 92-237;
99-200; 95-116

Dear Ms. Salas:

On August 8, 2001, Mary Brown, Chuck Goldfarb, Alan Buzacott, and I met with the following staff members of the Common Carrier Bureau to discuss the pending proceeding on universal service reform: Jack Zinman, Katherine Schroder, Anita Cheng, Paul Garnett, Greg Guice, and Jeff Waldau. We discussed the issues contained in the attached document, which was distributed at the meeting.

In accordance with section 1.1206(b) of the Commission's rules, 47 C.F.R. § 1.1206(b), an original and 11 copies of this memorandum and attachment are being filed with your office.

Sincerely,



Lori Wright
Associate Counsel

cc: Jack Zinman (w/o attachment)
Katherine Schroder (w/o attachment)
Anita Cheng (w/o attachment)
Paul Garnett (w/o attachment)
Greg Guice (w/o attachment)
Jeff Waldau (w/o attachment)

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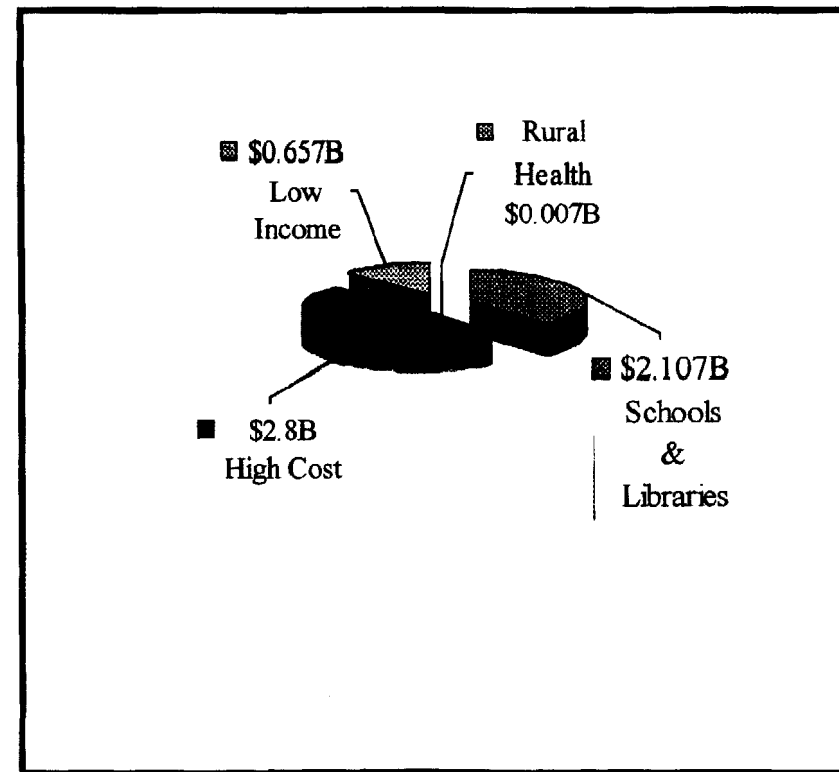
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The Current Universal Service Collection Mechanism Is Not Sustainable: Issues and Proposed Solutions



Federal Universal Service Fund : \$5.5 Billion per Year

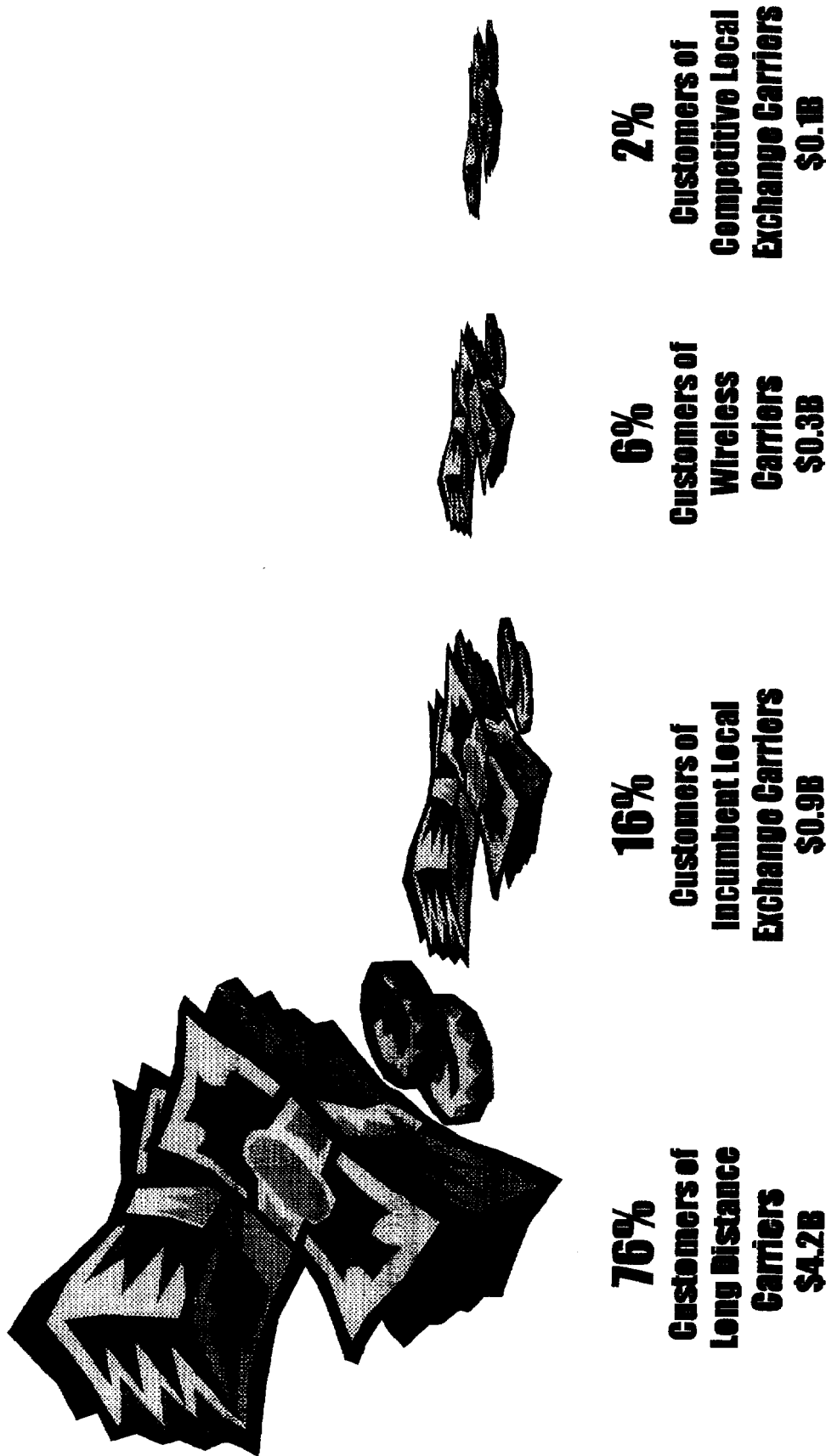
- High cost fund keeps rural rates affordable
- Low income households receive inexpensive Lifeline service and discounts for initial connection charges
- Schools and libraries receive e-rate discounts for equipment, wiring, and Internet connectivity
- Rural health care providers receive telecom discounts for telemedicine applications



\$5.5B Fund Will Continue to Grow

- **Bush administration projects \$7.9 billion by 2006**
- **Remand of FCC's Ninth R&O creates risk of larger fund**
- **Rural carriers asking for more – but without enforceable commitments to broadband deployment**
 - **“Multi-Association Group” wants to increase USF by as much as \$1 billion plus an annual inflation factor**
- **Fund could increase further if:**
 - **Definition of universal service is implemented by FCC to include advanced services**
 - **More eligible low income households participated**
 - **More customers in high cost areas acquired multiple lines**

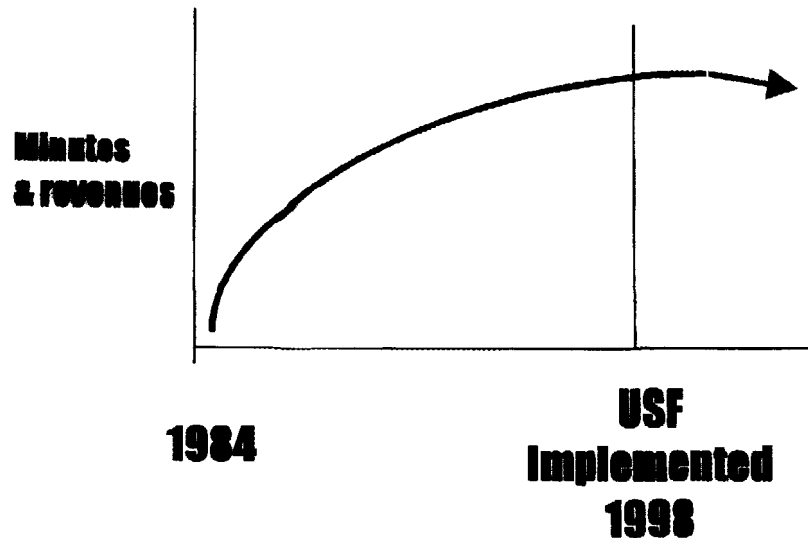
Who pays the \$5.5 billion? Customers!



How does the universal service fee appear on monthly customer bills?

- **Long distance customers: a percentage charge on revenues, in 8-9.9% range**
- **ILEC customers: a per line charge, typically in the range of \$0.35-\$0.45**
- **Wireless customers: a per line charge, typically in the range of \$0.40-\$0.53**

Fundamental change has occurred in the long distance market



- Long distance voice revenues are now in decline, and even minutes are declining for residential
- Glut in long-haul capacity put substantial downward pressure on prices
- Wireless successfully substituting for traditional long distance service
- Instant messaging and e-mail also are substitutes
- Future: Voice on Internet

With the amount to be collected by long distance carriers chasing fewer long distance minutes and revenues ...

... each remaining minute or dollar of revenue must bear a heavier burden.

The result -- *retail surcharges increase.*

Revenue-based system has measurement problems

- **Wireless carriers sell blocks of minutes, and cannot distinguish interstate from intrastate revenues**
 - **Use “default” allocator that understates interstate usage**
- **Most industry experts agree that carriers will increasingly sell certain “bundles” of interstate and intrastate services, CPE, enhanced services**

WorldCom's Proposal

- **Eliminate revenue-based assessment**
- **Replace with a connections and capacity assessment on the interstate telecommunications provider that “owns” the end user customer**

WorldCom's proposal: residential

- **USAC to assess carriers based on wireline and wireless interstate connections**
 - **\$1 per connection per month**
 - **Lifeline assessed nothing**
- **Pagers assessed at \$0.25 per month**

WorldCom's proposal: business

- **USAC assesses on interstate network connections and capacity**
 - **Single-line business (wireline and wireless) at \$1; pagers at \$0.25**
 - **Residual multi-line business (wireline and wireless) base charge \$2.50 - \$3.25:**

<u>Level</u>	<u>Facility Capacity</u>	<u>USF Contribution Rate</u>
1	Less than 1.544 Mb/s	Base multi-line business USF charge
2	1.544 Mb/s (T-1) up to 45 Mb/s	5 X (base MLB USF charge)
3	45 Mb/s (DS-3) or greater	40 X (base MLB USF charge)

Who pays under WorldCom's plan?

- **Carrier who “owns” the customer for the purpose of providing the connection is assessed**
 - **ILECs based on loops provided to their end users (loops are legally considered interstate, as well as intrastate)**
 - **Competitors who provision end users from their own loop facilities, via UNE-P or unbundled loop, or using interstate special access**
 - **Wireless carriers based on the number of “connections” (more easily counted than interstate revenues)**

Advantages

- **Competitively and technology neutral**
- **As network evolves from PSTN to Internet, system based on connections is stable and predictable**
- **No need to assess dot.coms for VoIP revenue**
 - **Revenue allocation issues – an unploughed field**
- **Facilitates flat fee recovery**

Proposal complies with the Act

- **Upon whom should the obligation to contribute to universal service fall?**
 - **“All interstate telecommunications providers”**
- **How should contribution be apportioned among interstate telecommunications providers?**
 - **Not prescribed by the statute; assessment must be equitable and nondiscriminatory**
- **No conflict with 5th Circuit decision**

Recovery of USF Contributions

- **Pass through plus administrative costs and uncollectibles**
- **FCC could set forth a “safe harbor” amount for administrative costs and uncollectibles**
 - **These costs will vary by carrier**

Recovery of USF Contributions, cont'd

- **Lifeline consumers pay zero in USF surcharges**
 - **Carrier providing connection knows who its lifeline customers are**
- **Surcharge name**
 - **Due to billing systems limitations, allow names similar to, but shorter in length than, “Federal Universal Service Charge,” e.g., Fed Universal Svc Charge.**

Need to move expeditiously

- **Every financial quarter, interstate revenues decline**
 - **AT&T year over year revenues decline in 2Q01 was 5.9%, including residential decline of 19.8%**
 - **WorldCom business voice revenues declined 6% 2Q01 vs 1Q01 and residential declined 16+%**
- **Increases in interexchange customer fees are not a helpful foundation for future health of universal service system**